use Class B accounts because Class A accounts are not essential for any federal regulatory purpose that needs to continue in the current environment. Any regulatory mechanisms that happen to rely on Class A accounting information should be reviewed pursuant to Section 11 standards to determine whether reliance on Class A accounting detail is no longer necessary in the public interest. The fact that certain regulatory mechanisms have been designed based upon Class A accounts should not be used as a pretext to avoid simplification of the accounting requirements. Instead, consistent with the Section 11 requirement that the Commission review all of its regulations, the Commission should review any such regulatory mechanism that relies on Class A accounting detail to determine whether that reliance is essential. Specifically, the current biennial review pursuant to Section 11(a) should include a review of the current pole attachment rules to determine whether they can be simplified to maintain the necessary degree of oversight of disputes concerning pole attachment rates while imposing less administratively burdensome obligations. In the few areas where the current pole attachment formulas use Class A accounting information, this review of the pole attachment rules should consider what alternative method could be used to review pole attachment rates, when necessary, to determine whether they exceed the maximum rate permitted by Section 224.

In any event, even without a biennial review of the pole attachment formulas, any ILEC opting to use Class B accounts could simply maintain equivalent internal accounting data necessary to calculate the components of the pole attachment formulas that currently use Class A accounts. To the extent necessary, during the biennial review of the pole attachment rules, the Commission could specify in terms of types of costs, rather than Class A account numbers, the method of calculating each of the components. In the alternative, the Commission should consider whether the pole attachment formulas could be converted to Class B accounts using

prorations to estimate the portion of each pertinent Class B account attributable to the pole attachment. In fact, some components of the pole attachment formulas, such as administrative costs, are already based on methods of approximating the actual cost attributable to poles.

IV. ALL ILECS SHOULD BE PERMITTED TO SUBMIT A CLASS B CAM.

The NPRM tentatively concludes that mid-sized ILECs should be permitted to use a Class B CAM.[35] Use of a Class B CAM goes hand-in-hand with use of Class B accounts. It logically follows from the conclusion to allow use of Class B accounts that the CAM should also be based on Class B accounts. Otherwise, much of the simplification obtained by permitting use of Class B accounts would be lost. That is, if the Commission permitted use of Class B accounts, but required a Class A CAM, then the ILEC really would not have the option of using Class B accounts.

The same reasoning that supports permitting all ILECs to use Class B accounts also supports permitting all ILECs to maintain their CAMs based on Class B accounts. The NPRM proposes to limit relief to the mid-sized ILECs because of its mistaken belief that there is a greater risk of cross-subsidy in the case of the largest ILECs. However, as the SBC LECs explained above, price cap regulation is the primary deterrent against cross-subsidy in the case of price cap ILECs. Further, in addition to price cap regulation, control of cross-subsidy is dependent on an ILEC's CAM, its internal control structures and its reporting procedures, none of which depend on the Part 32 level of detail. Control of cross-subsidy is independent of the level of detail in the Part 32 accounts. Class A accounts are simply not the basis for cost allocation in the ILEC CAMs. Rather, the allocation of costs in accordance with the Joint Cost

[35] NPRM, ¶ 10.

Order's hierarchy of cost allocation procedures is performed on a cost pool basis, which do not require the specific categories in the detailed Class A set of accounts. As a further example, in many cases, outside plant accounts are directly assigned to regulated operations, and thus, dividing the plant into numerous Class A account categories does not change the accuracy of the cost allocation at all. Even in those accounts where there are common cost pools and direct nonregulated cost pools, those cost pools can continue to be maintained even if they are organized under the Class B set of accounts. Class B reporting would permit more flexible accounting while continuing to fully satisfy the Part 64 cost allocation requirements.

Since the maintenance of Class A accounts makes no difference in the accuracy of cost allocation or the prevention of cross-subsidy, there is no reason to limit the relief from Class A accounting requirements to the mid-sized ILECs, as the NPRM proposes. For the same reasons discussed previously, the Commission should permit all ILECs to maintain and submit their CAMs based on Class B accounts. Given that a Class B CAM is just as effective as a Class A CAM and the largest ILECs are subject to price cap regulation without a sharing mechanism, as well as a higher degree of local exchange competition, it would be unreasonable and arbitrary to permit mid-sized ILECs, but not the largest ILECs, to use a Class B CAM.

V. THE BURDEN OF THE ACCOUNTING AND COST ALLOCATION REQUIREMENTS IS SIGNIFICANT AND SHOULD BE REDUCED IN VIEW OF THE MINIMAL BENEFIT OF THESE REQUIREMENTS.

The accounting and cost allocation requirements have outlived their usefulness in accomplishing many of the original objectives for which they were adopted. The Part 32 accounting requirements were adopted at a time when the Commission needed this level of detail for purposes of cost-based rate-of-return regulation of ILECs' rates for interstate services. The advent of price cap regulation, and the removal of the sharing mechanism, have largely

eliminated the Commission's reliance on, and thus the importance of, embedded costs as detailed in Part 32.[36] Part 32 was also adopted at a time when ILECs faced little, if any, competition for their local exchange business. The competitive environment has changed dramatically, especially in urban areas and even more acutely in the large metropolitan areas served by the largest ILECs.

When Part 32 was adopted, the Commission viewed it as a financial accounting system that would serve both the Commission's regulatory needs and the carriers' management information requirements.[37] However, in the changed competitive environment, Part 32 does not serve management's information needs at all and it largely no longer serves the Commission's regulatory needs.[38]

The NPRM tentatively concludes that because ILECs maintain financial records in much greater detail than the Class A requirements, "the burden on the largest incumbent LECs resulting from Class A accounting and reporting requirements does not outweigh our needs for collecting financial information."[39] The NPRM exaggerates the benefits of the Class A accounting detail and underestimates the burden of complying with the Part 32 accounting requirements. Part 32 requires ILECs to maintain a rigid, structured Class A chart of accounts

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[36] See Price Cap Order, ¶ 152.

[37] 47 C.F.R. § 32.2(f).

[38] Arthur Andersen LLP, "Accounting Simplification in the Telecommunications Industry" 1998, filed on July 15, 1998 §§ IV, at 14-21 (the "Arthur Andersen Whitepaper").

[39] NPRM, ¶ 6. Since all ILECs maintain detailed internal financial records for management purposes, the internal records maintained by mid-sized ILECs as compared to the largest ILECs is not a basis to distinguish the two groups.

for regulatory accounting purposes. While it is true that ILECs maintain internal financial records in greater detail than the Class A details, the type of detail maintained for internal purposes is different from that required by the Class A accounts. The burden of Part 32 is the requirement to develop and maintain a different set of details for regulatory purposes that ILECs do not need for their own internal management purposes. The ILECs are not able to use the Class A accounting details to produce information they need for management purposes. Therefore, the result is that ILECs must maintain duplicate sets of detailed accounting information, one for management purposes and the other for regulatory accounting purposes.

Consequently, the fact that ILECs maintain detailed internal financial information does not reduce at all the burden imposed by the Class A accounting requirements. In fact, the greater the differences between the internal financial records and the Part 32 records, the greater the burden on the ILECs to maintain the two parallel sets of detailed records. The reason is that there is a higher cost of mapping information from the Part 32 records to the management financial records and reconciling differences between the two sets of records. In some cases, an ILEC may choose to compromise its need for management information by settling for the inferior data supplied by the Class A accounts, when its ability to manage would be enhanced by having the flexibility to design its accounts and subaccounts in a manner that would provide more meaningful information for management purposes.

Thus, the Class A accounting rules limit the flexibility of ILECs in designing their accounting systems in a manner that will best enable them to manage their business in a competitive environment. In addition, the Class A accounting requirements impose the additional costs of tracking expenses to the more detailed accounts and expense categories of the Part 32 Class A books.

The burden of maintaining Class A accounting details is significant, as evidenced by the larger number of employees that the largest ILECs need to keep the two "sets of books" and underlying records compared to the number of employees that comparable companies use to maintain their nonregulated accounting systems.[40] For example, Arthur Andersen shows that the ILECs it reviewed employ up to 60% more staff to maintain their charts of account compared to similar companies in other capital-intensive industries.[41] Other unnecessary Part 32 requirements also impose extremely high costs on the ILECs. For example, according to Arthur Andersen, five of the largest ILECs must have almost 100 more employees on their staffs (on the average) to manage their fixed assets and depreciation accounting compared to capital-intensive companies that are not subject to Commission regulation.[42]

While the amount of cost savings is difficult to measure precisely, ILECs are at an undeniable disadvantage compared to their competitors because they do not have the flexibility to design their accounting and recordkeeping systems efficiently to manage their business. Instead, they are required to maintain a redundant, unnecessary set of accounting details and records solely for reporting purposes (i.e., that detailed data no longer directly affect rates).

Given that Part 32's usefulness in accomplishing any of the Commission's regulatory objectives is very limited under price cap regulation in a competitive local exchange environment, the necessity of maintaining the Class A accounting details and other Part 32 requirements are far outweighed by their burden, especially for price cap ILECs. Even though

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[40] Arthur Andersen Whitepaper, § IV, at 20.

[41] Id.

[42] Id. at 32.

simplification is especially justified for price cap ILECs, the SBC LECs submit that the Commission should eliminate the Class A accounting requirements for all ILECs, as well as relieve them from other burdensome Part 32 requirements, such as the detailed property recordkeeping and depreciation requirements. In fact, the benefit of maintaining Class A accounts versus Class B accounts is virtually nil because many of the regulatory mechanisms that rely upon accounting information will be just as effective using Class B accounts as they are using Class A accounts. For example, as discussed above, the Part 64 cost allocation rules will be able to continue accurately and effectively allocating costs between regulated and nonregulated activities even after transition from a Class A to Class B accounts. Given the sufficiency of Class B accounts to perform the Commission's existing regulatory functions, there is no need to continue imposing the burden and inefficiencies of Class A accounts. Ultimately, as the Commission proceeds with its Section 11 review and eliminates other regulatory functions that are no longer necessary, even Class B accounts can be eliminated.

VI. ALL ILECS SHOULD BE PERMITTED TO PERFORM THE PART 64 INDEPENDENT CAM AUDIT EVERY TWO YEARS, INSTEAD OF ANNUALLY.

While the long-term goal should be to reduce the burden of all audits not expressly mandated by the Communications Act, as a transitional deregulatory measure, the burden of the Part 64 independent audit should be reduced by allowing biennial rather than annual audits. The deregulatory relief from annual independent CAM audits should not be limited to the mid-sized ILECs as proposed in the NPRM.[43] Instead, the proposed streamlining of the Part 64 independent audit should apply to all ILECs. The largest ILECs are subject to price cap

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[43] NPRM, ¶ 11.

regulation, without any sharing mechanism, and thus, Part 64 cost allocation plays a minimal role in preventing cross-subsidy. Given the reduced importance of cost allocation rules in the prevention of cross-subsidy, annual independent CAM audits are also far less important than when they were adopted for purposes of traditional rate-of-return regulation. Likewise, an attest audit is more than sufficient for the Commission's current purposes in regulating any ILEC.

There is simply no reason to continue performing these intensive audits every single year regardless of the burden and expense imposed on the ILECs. Periodic audits, such as every two years, using the attestation standards, would be far more efficient and would practically cut the resources used in half.

Since a number of the mid-sized ILECs have not opted to use price cap regulation, the reduction of the audit burden is actually less justified for the mid-sized ILECs compared to the largest. However, as measured against the incremental anticipated benefits of the existing audit requirements, the relative degree of the burden of independent audits justifies relief for the mid-sized ILECs, just as price cap regulation justifies relief for the largest ILECs.

VII. CONSOLIDATION OF EQUIPMENT ACCOUNTS 2114-2116 AND EQUIPMENT EXPENSE ACCOUNTS 6114-6116 IS THE TYPE OF CONSOLIDATION THAT THE SECTION 11 REVIEW SHOULD EXTEND THROUGHOUT PART 32.

USTA recommended a number of changes to streamline Part 32 in a letter dated February 19, 1998 to the Accounting Safeguards Division. Out of the numerous changes presented by USTA and several ILECs, including the SBC LECs, for purposes of the Section 11 Biennial Review, the NPRM has selected only one token recommendation involving the equipment recorded in Accounts 2114-2116.[44] Specifically, the NPRM proposes to consolidate accounts

[44] NPRM, ¶ 14.

2114-2116 into a single equipment investment account and Accounts 6114-6116 into a single equipment expense account. While the NPRM indicates that, unlike the Class B accounting proposal, the changes proposed in Section II of the NPRM "will apply to all carriers subject to Part 32 and not just the mid-sized incumbent LECs,"[45] these particular changes would be irrelevant to any mid-sized ILEC that opts to use the Class B accounts because under the Class B accounts, Accounts 2114-2116 are consolidated along with six other accounts into a single Class B account, Account 2110. Instead of this meager relief for the largest ILECs, all ILECs should be permitted to use Class B accounts.

In an event, this type of consolidation is worthy of consideration for purposes of those ILECs that do not opt to use the Class B system of accounts. However, the quantity of assets in Accounts 2114-2116 is *de minimis* (perhaps 1% or less). Therefore, the reduction in burden achieved by this consolidation would be barely noticeable. In order to yield meaningful deregulatory results, this same type of consolidation should be carried throughout Part 32. It could be done without any adverse consequences. In fact, the logical extension of applying the same type of deregulatory analysis throughout Part 32 would be to permit all ILECs to use Class B accounts. As part of its "attic-to-basement" review of accounting rules pursuant to Section 11, the NPRM should consider all of USTA's proposals as well as those set forth in SBC's Section 11 Petition.[46]

Accounts 2114-2116 can be consolidated without any adverse consequences. There is no need to separately identify the three types of equipment now reported in these three accounts.

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[45] NPRM, ¶ 13.

[46] See Exhibit 1 to these Comments.

The same can be said with regard to other groups of accounts in the Class A system of accounts. Now that ILECs are no longer rate-base regulated and are market and customer driven, their management is more interested in an accounting system arranged around marketing segments and classes of services, rather than the functions causing expenses.

If Accounts 2114-2116 can be consolidated, there is no reason that the same analysis would not produce a consolidation of other groups of accounts, perhaps up to and including the Class B level. However, assuming that a Class A accounting system continues to be used by some ILECs, the Commission should consider consolidating other accounts, such as the following switching accounts: Accounts 2211, 2212 and 2215. Likewise, the Commission should consider consolidating the related switching expense accounts. There is little if any remaining benefit in distinguishing different types of switching technologies by using separate accounts, especially when some of these technologies are quickly becoming obsolete, if not already a dying account in many jurisdictions. Consolidation of these accounts would eliminate the need to keep separate Class A accounting records for obsolete technologies. Since the switching accounts have about a fifth of the SBC LECs' investment, this consolidation would provide a more meaningful measure of relief from the Class A accounting burden.

Another example of a consolidation that is worthy of consideration would be the consolidation of the following cable and wire accounts into a single account: 2421-2426 and 2431. While distinctions between types of cable may be important for internal engineering purposes, it is not necessary to maintain these distinctions for financial accounting or reporting

purposes.[47]

For purposes of the consolidations of groups of accounts, the Commission's depreciation practices should not be the controlling criterion because the Commission's depreciation rules also need to be reviewed pursuant to Section 11 and, as a result of that review, depreciation differences between similar accounts should no longer be relevant.

The NPRM indicates that there are two reasons for consolidating Accounts 2114-2116: the similarity of depreciation rates and the identical treatment under the Part 36 jurisdictional separation rules.[48] The same circumstances are presented in the case of other groups of accounts. However, the similarity of depreciation rates should not be viewed as essential for the consolidation of other accounts. The Commission should ignore the previously prescribed depreciation rates in deciding whether to consolidate accounts because ILECs should be relieved of the Commission-prescribed depreciation rates and allowed to set their own depreciation rates based on superior economic analysis consistent with GAAP. And, since there is only one isolated difference between the jurisdictional separations rules for Class A and Class B accounts,[49] the Part 36 separations rules also need not play any part in deciding whether to consolidate accounts.

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[47] As a further example of the type of consolidation that could be carried throughout Part 32, Accounts 4340 and 4341 can be consolidated without sacrificing any regulatory benefit. The net effect of the difference between federal/state deferred taxes and taxes related to Part 32 flow-through items could be journalized as an asset (1437) or liability (4361). See Letter dated March 12, 1998 from Gerald Asch, Directory Federal Regulatory, Bell Atlantic, to José Rodriguez, FCC, Attachment E.

[48] NPRM, ¶ 14.

[49] See n. 16 supra.

Instead of the "drop-in-the-bucket" approach reflected in the NPRM's limited proposal to consolidate only 6 out of 261 accounts (or less than 3% of all accounts), the Commission should undertake a comprehensive review of each and every group of accounts in Part 32 to assess whether the same detailed categories are still necessary for those ILECs that continue to use Class A accounts. Under a proper Section 11 analysis, the Commission's review should begin with the proposals that have been submitted pursuant to Section 11, including SBC's Section 11 Petition and USTA's recommended changes submitted on February 19, 1998 and in its Comments being filed in this proceeding.

VIII. ALL NONREGULATED REVENUE SHOULD BE RECORDED IN A SINGLE ACCOUNT (I.E., ACCOUNT 5280).

The NPRM tentatively concludes that revenue from all nonregulated activities should be recorded in a single account, Account 5280, as sought in USTA's petition for rulemaking filed on September 16, 1997.[50] As more fully explained in the SBC LECs' comments on USTA's petition for rulemaking, the SBC LECs are in full agreement with the proposal to consolidate all nonregulated revenue in a single account, Account 5280, and to make the other necessary changes consistent with that consolidation of revenues.[51] There is simply no reason to require disaggregated reporting of the revenue from different types of nonregulated activities. In fact, the Commission previously appeared to reach the same conclusion when it stated "we have no

[50] NPRM, ¶ 16.

[51] See Comments of Southwestern Bell Telephone Company, Pacific Bell and Nevada Bell, AAD Nos. 97-103 and 97-104, filed November 3, 1997, at 1-5 and Exhibit "A".

regulatory need for service-specific revenue data for nonregulated activities. Our regulatory purposes are satisfied by using a single account for this purpose."[52]

Given that the Commission has effectively only given ILECs relief from separate accounting and reporting of payphone revenue, by granting USTA's request for a waiver, the Commission should expeditiously finalize its action with respect to all types of nonregulated revenue. This final action would eliminate the current uncertainty concerning future reporting of nonregulating revenue.

IX. ILECS SHOULD BE PERMITTED TO IMPLEMENT CHANGES IN ACCOUNTING STANDARDS AUTOMATICALLY.

Section 32.16 appears to require carriers to adopt new accounting standards promulgated by the Financial Accounting Standards Board ("FASB") pursuant to GAAP, and yet, it contains conditions that ILECs must satisfy before adoption of such standards, including a built-in delay of at least 90 days as well as a cumbersome requirement to prepare a detailed study concerning the revenue requirement impact for the current year as well as a projected impact for the following three years. The NPRM proposes to reduce the burden of Section 32.16 by eliminating the requirement to provide a projection of the impact over the three years following implementation.[53]

Price cap ILECs should be permitted to adopt new accounting standards prescribed by the FASB without any requirement to notify, or obtain approval from, the Commission.

In particular, revenue requirement studies have practically no relevance for price cap

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[52] Order on Further Reconsideration, CC Docket No. 86-111, 3 FCC Rcd 6701, ¶ 13 (1988).

[53] NPRM, ¶ 17.

carriers, especially now that the Commission has eliminated sharing. Under price cap regulation, a change in accounting standards that results in a change in costs does not have any impact on the ordinary rate-setting process. Since there is no regulatory benefit to be served by requiring studies of the financial impact of new accounting standards in the case of price cap ILECs, the burden of Section 32.16 is clearly not justified by any regulatory benefit.

In fact, Section 32.16 is burdensome not only because it requires preparation of irrelevant studies in the case of price cap ILECs, but also because it delays implementation of new FASB accounting standards or impedes implementation of those standards in the most cost effective manner. Faced with the obstacles presented by Section 32.16, an ILEC has two choices. First, it can delay implementation until after it satisfies the burdensome requirements of Section 32.16. In the alternative, the ILEC can proceed to implement the standard for purposes of its external financial reporting, while continuing to maintain the Part 32 books of account as if the new accounting standard had not been adopted. The former alternative causes delay in implementing the FASB changes and the second alternative creates additional unnecessary and burdensome recordkeeping differences between the Part 32 set of books and the external financial reporting. Ideally, for price cap ILECs, the Commission should allow automatic adoption of new accounting standards prescribed by FASB for Part 32 accounting and reporting purposes, as this would allow ILECs to implement such GAAP changes in the most cost-effective manner. At a minimum, however, price cap ILECs should not be required to perform any revenue requirement studies.

X. A COMPREHENSIVE SECTION 11 REVIEW OF THE PART 32 RECORDKEEPING REQUIREMENTS SHOULD RESULT IN ELIMINATION OF MANY REQUIREMENTS, ESPECIALLY FOR PRICE CAP ILECS.

There are many aspects of Part 32 accounting requirements that the Commission should review as part of a proper, comprehensive review of all regulations pursuant to Section 11. The property recordkeeping and depreciation requirements are among the most burdensome of the Part 32 requirements, and thus, certainly should not be overlooked in performing the biennial review process.[54]

In contrast to such a comprehensive biennial review, the NPRM barely scratches the surface of the Part 32 recordkeeping requirements by proposing to eliminate a recordkeeping approval requirement in Section 32.2000(b) that ILECs are seldom required to use.[55] In particular, the NPRM proposes to eliminate the approval requirement for journal entries associated with acquisitions of plant from other companies. While the SBC LECs agree with the NPRM's tentative conclusion that this approval requirement should be eliminated, this is not even the "tip of the iceberg" among the excruciatingly detailed journal entries and other records required by Part 32 as applied to ILECs.

Certainly, the plant acquisition approval requirement should be eliminated because it serves no useful regulatory purpose in today's regulatory and competitive environment, especially as applied to price cap ILECs. To the extent that there is any reason for the

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[54] The SBC LECs acknowledge that the list of 31 proceedings released by the Commission on February 5, 1998 included a separate item relating to the depreciation rules. See News Release, Report No. GN 98-1, February 5, 1998. Thus, these Comments do not focus on the long-overdue depreciation simplification.

[55] NPRM, ¶ 18.

Commission to review acquisitions of plant, the Commission always has the option of obtaining additional data to the extent necessary at the time of the purchase. The NPRM bases its tentative conclusion on other accounting safeguards such as ARMIS reporting and the Commission's audit program. However, with respect to price cap ILECs, price cap regulation and the ability to obtain additional data are alone sufficient to serve any remaining regulatory needs the Commission may have in connection with such sales transactions. The lack of any benefit in the case of price cap ILECs is clear from the NPRM's description of the reason for this requirement. The NPRM states that this requirement helps ensure that the ILEC "does not inflate the rate base or allow recovery of depreciation expense already recovered by the previous owner of the plant."[56] However, under price cap regulation without a sharing mechanism, the ILEC cannot increase its rates by virtue of its purchases of plant. The rate base and depreciation expense do not play much, if any, part in the rate-setting processing under price cap regulation. Therefore, the requirement does not serve any federal regulatory purpose under price cap regulation.

The Commission should review all of the other Part 32 recordkeeping requirements and weigh the burden of these requirements against any identifiable benefits that the Commission realistically expects to achieve by continuing to apply those requirements. The SBC LECs submit that there is no further benefit in requiring price cap ILECs to maintain property records at an excessive level of detail. As explained in SBC's Section 11 Petition, all of the Part 32 property record requirements should be eliminated for price cap ILECs; instead, price cap ILECs should be allowed to rely solely on the requirements of GAAP.[57] The Arthur Andersen

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[56] NPRM, ¶ 18.

[57] SBC's Section 11 Petition at 11-13, & Exhibit B. See also Exhibit 1 to these Comments.

Whitepaper explains why price cap ILECs should not be required to keep detailed records concerning millions of individual property record units, including those of extremely small value.[58] According to Arthur Andersen, each of the largest ILECs must keep track of over 50 million individual property units under Part 32 compared to generally less than one million for a comparable nonregulated company, such as one of the ILECs' competitors.[59] The recordkeeping costs for a large share of property record units exceeds the value of the items of equipment. Price cap ILECs should have the flexibility to manage their investment using GAAP in the same manner as their competitors and companies in other industries. As a transitional measure toward complete relief from the regulatory burden of the recordkeeping requirements, the Commission should at least adopt Arthur Andersen's recommendations[60] and allow price cap ILECs to define their property record units so that they need not separately identify low-value network assets. As the Arthur Andersen Whitepaper shows, ILECs incur several times the cost incurred by companies in other industries in maintaining records of this type. For example, Arthur Anderson estimates that, compared to other capital-intensive businesses that are not regulated, ILECs employ four times as many persons to perform property recordkeeping.[61] Requiring ILECs to

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[58] Arthur Andersen Whitepaper, § V, at 25-37. Among other things, Arthur Andersen shows the excessive of the Part 32 recordkeeping compared to other capital-intensive industries: "For example, in the airline industry, the relevant property units are engines and airframes – within the airframes category, the seats, carpeting, wings, instrument panels, etc. are not tracked nor retired as separate units of property." Id. at 33.

[59] Id. at 32.

[60] Id. at 32-37.

[61] Id. at 32.

keep track of fifty times as many units of property as their competitors at up to four times the cost, and for no apparent reason in the case of price cap ILECs, has a crippling effect on the ILECs' ability to compete efficiently with those who are not burdened by these requirements.

Instead of the "tip-of-the-iceberg" approach of the NPRM, the Commission should undertake a comprehensive review of all of the Part 32 recordkeeping requirements with a view to eliminating not merely those requirements that are seldom applicable, but, instead, all of the antiquated rate-of-return recordkeeping requirements that impose daily burdens on numerous employees at each of the ILECs.

XI. CONCLUSION.

Instead of continuing to hold onto these vestiges of rate-of-return regulation of ILECs' book and records, the Commission should adopt a forward-looking blueprint to guide its regulation in areas such as this. To properly consider competition, and the resulting changes in the public interest analysis, this roadmap must be designed not only based on the unprecedented changes in the industry since the last comprehensive review of the accounting and cost allocation rules over ten years ago, but the changes that are anticipated in the months and years to come. Rapid technological evolution, adoption of price cap regulation and similar forms of incentive regulation at the federal and state levels, emergence and spread of competition in the local exchange market, passage of the 1996 Act, emergence and rapid growth of Internet, data communications, wireless and other products and services and other revolutionary changes should combine to create a roadmap that involves a more moderate form of regulation in many areas, especially accounting. Such regulation should be designed in a more efficient manner to

accomplish only essential regulatory tasks(to monitor only to the extent strictly necessary), while reducing the burden of regulation on ILECs to permit ILECs to manage their accounting at a level more comparable to their competitors and members of other industries.

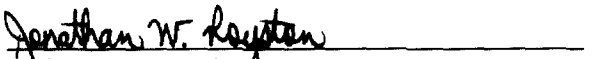
While the ultimate goal should be to permit all ILECs the flexibility to use the same kinds of accounting and recordkeeping practices followed by their competitors and members of other industries, relying solely on GAAP, the Commission should proceed to an intermediate step along this route by adopting the short-term deregulatory measures described in these Comments and in SBC's Section 11 Petition. To properly carry out the mandate of Section 11, the Commission needs to consider all of these recommendations, as well as those presented by USTA, Arthur Andersen and other parties.

The Commission should not limit relief to an arbitrarily selected class of carriers such as the mid-sized ILECs. Instead, the deregulatory review required by Section 11 should consider to what extent any of the Part 32/64 requirements are still necessary for any carrier, regardless of its size or circumstances. The Commission should be especially careful to avoid creating arbitrary classifications, such as continuing to regulate where deregulation is most justified (price cap ILECs subject to greater local competition) while deregulating where some continuing regulation may be justified (rate-of-return mid-sized ILECs not subject to local competition).

For the foregoing reasons, the SBC LECs urge the Commission to perform the comprehensive review of all accounting and cost allocation rules as applied to all ILECs as described in these Comments.

Respectfully submitted,

SOUTHWESTERN BELL TELEPHONE COMPANY
PACIFIC BELL
NEVADA BELL



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PART 32 SIMPLIFICATION ISSUE

RECORDKEEPING REQUIREMENTS

- Eliminate detailed instructions and procedures for maintaining retirement units and property records.
- Eliminate requirement to file retirement units list.
- Recognize gain or loss on disposition of plant immediately which is more in line with traditional GAAP treatment of fixed asset retirements.

PROPOSED ALTERNATIVE AND ANALYSIS

Relaxing the recordkeeping detail in Part 32.2000 would significantly reduce costs by decreasing (1) the amount of time administering the current level of detail and (2) the computer storage and systems maintenance.

This will make Carrier financial statements more consistent with financial statements and calculated financial indicators of the unregulated industry at large. There should be a goal for LECs to employ GAAP techniques as employed by industry at large to enhance financial comparisons between regulated carriers and the remaining portions of outside industry.

Under price caps, amounts carried in the rate base no longer bear a direct relationship with rates charged to customers. As such, there should no longer be such an extensive need to provide reams of cost data to support the rate setting process for price cap carriers.

Carriers should be allowed to maintain records in conformance with GAAP and establish internal controls that satisfy standards set by SAS auditing statements. GAAP does require certain accounting records to be created which support the

existence of a company's fixed assets. This record keeping in most instances is significantly less than that called for by the Part 32.2000 rules for plant but nevertheless still demonstrates and supports the materially correct balances of the fixed assets.

USOA STRUCTURE

- The long term goal concerning the accounts structure should be to eliminate the text which specifies the detailed accounting instructions in the Part 32 rules. This would significantly streamline and simplify the Part 32 rules.
  Carriers should be afforded the long term goal of utilizing Generally Accepted Accounting Principles as the guide for accounting methods, principles, and dictates in providing the financial information for a price cap carrier.

As explained above, there are good reasons for promulgating the use of GAAP within the LEC industry and price cap carriers in particular.

- In the interim as a transitional step toward GAAP, SBC believes that it as well as other Tier 1 price cap carriers should be provided the flexibility to employ the Class B accounting rules in satisfying the financial accounting needs called for in the Code of Federal Regulations i.e. Part 32,36, and 64. These rules are currently employed by Tier 2 LECs.

Class B accounting satisfies all requirements in reporting Part 36 and 64 information as is obvious by the fact that Tier 2 carriers do employ this aggregated account structure. To the extent it continues to be necessary, jurisdictional rate of return calculations can be developed to produce the interstate rate of return (492 report) as well as state rates of return when needed.

Class B accounting significantly reduces many burdensome reporting activities since there are 105 accounts in lieu of the 233 accounts in Class A. This significantly eases the reporting process of the major ARMIS financial reports (43-01,43-02, 43-03, and 43-04) .

This also allows the carrier to make significant reductions in various administrative, financial, and operational processes and systems due to the lesser amount of account data needed. For instance, time reporting can be simplified in the field or perhaps modified to capture data that is more conducive to effectively completing field

operations in lieu of capturing data from an account structure that has not changed meaningfully in at least a decade. In the case of a price cap carrier setting rates based upon Price Cap Indices,
it is no longer relevant to separately identify and report items such as 6722-external affairs, 6531-power expense, 6424-Submarine Cable Expense, 6431-aerial wire expense etc.

- Eliminate all requirements for specific subaccounts and subsidiary records.

Subsidiary level detail is not useful for internal or external purposes and is costly to maintain. For example, it is no longer necessary to separately identify items such as 2215.1- Step by step, 2215.2- Cross Bar, and 2215.3- Other Electromechanical switching.

- Permit carriers to establish expense limit based on GAAP.

Price cap carriers should be allowed to utilize the same judgment and discretion as the general business community in setting the limits (or threshold) at which purchases are determined to be an expense and not an asset. After a lengthy proceeding, the FCC ordered an increase in this expense limit to $2000 for support assets which are a minor part of the overall asset base. The $2000 limit might be considered a reasonable industry benchmark to use for the asset base and an appropriate one but it took far too long for this new expense limit to be approved by the FCC. The industry worked with the FCC on this initiative from 1992 through 1997. Typically, in the general business community, this is a decision that can be made in a matter of weeks after consultation with an outside accounting firm. Moreover, there is no benchmark for expensing network items which continue to be individually tracked. This requires a large investment in time to administer inventory techniques and system resources to continue to identify items which do not have a significant value.

- Permit carriers to establish materiality standards based on GAAP.

Part 32.26 effectively prescribes that materiality based upon GAAP standards should have no bearing in following the Part 32 system of accounts.

GAAP and SEC regulations generally combine to permit a limited zone of materiality within which exact treatment or conformance of a particular accounting transaction or group of accounting transactions according to a particular GAAP

principle or to past accounting policy is not challenged. This permits companies to avoid wasting inordinate amounts of time revising or changing very small accounting transactions which have no meaningful bearing on the overall financial picture or results. Part 32 should embody this concept.

DEPRECIATION ACCOUNTING

- Permit carriers to set their own depreciation and amortization rates and processes.

Telecommunications Act of 1996 permits forbearance from FCC depreciation rate setting mechanisms.

Carriers should be permitted to set depreciation rates based on economic analysis consistent with GAAP i.e. simple estimates of the life of plant investment.

The current represcription process is micromanaged using a morass of historic retirement information and outdated principles. Useful and usable information is available from outside consultants which can be easily transcribed into the development of depreciation rates. SBC supports techniques such as this to geometrically streamline the rate represciption process.

Depreciation changes are endogenous under current Price Cap rules. As such, price cap carriers do not alter price cap rates to recognize changes in the estimated lives of plant.

NOTIFICATION REQUIREMENTS

- Permit carriers to implement changes in

Allow carriers to follow accounting conventions used by the interexchange carriers and other outside industries. Afford carriers the opportunity to use the same GAAP